



SMALL PUBLIC COMPANY
COALITION

May 27, 2022

VIA ELECTRONIC MAIL

Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-0609

Re: Further Definition of “As a Part of a Regular Business” in the Definition of Dealer,
File No. S7-12-22

Dear Ms. Countryman:

The Securities and Exchange Commission has asked whether there are “standards of activity other than the standards under the Proposed Rules that the Commission should apply in the context of analyzing dealer status.” *Further Definition of “As a Part of a Regular Business” in the Definition of Dealer*, 87 Fed. Reg. 23,054, 23,077 (Apr. 18, 2022). The Small Public Company Coalition (SPCC) appreciates the opportunity to comment on this important question. The answer is yes, and those standards should be based, as they must, on the statute itself.

In recent years, the Commission’s enforcement Staff has advocated a novel and radically expansive view of the Commission’s authority, under which *any* business that buys and sells securities for profit is a securities “dealer” required to register with the Commission. *See, e.g.*, SEC Mem. in Opp’n to Defs.’ Mot. for Summ. J. 7, *SEC v. Almagarby*, No. 17-cv-62255 (S.D. Fla. Nov. 4, 2019), ECF No. 79 (“purchasing and selling securities” in “more than a few isolated transactions” is sufficient to require dealer registration); *id.* at 8 (arguing that the court “need look no further” in assessing dealer status, because the defendant’s “business model was based entirely on the purchase and sale of securities”). In pressing this sweeping theory, the enforcement Staff has written off the Commission’s prior guidance as “not dispositive,” *id.* at 12, and insisted that the presence of investor “customers” or the offering of typical “dealer services” is not relevant to the analysis, SEC Opp’n to Defs.’ Mot. for J. on Pleadings 25, 28, *SEC v. Carebourn Capital, L.P.*, No. 21-cv-2114 (D. Minn. Mar. 10, 2022), ECF No. 57. A number of lower courts have accepted the Staff’s theory without substantive analysis. *See, e.g.*, *SEC v. Carebourn Capital, L.P.*, 2022 WL 1639515, at *4 (D. Minn. May 24, 2022) (holding that a “high volume of buying and selling securities” indicates that dealer “registration is required”); *SEC v. GPL Ventures LLC*, 2022 WL 158885, at *5 (S.D.N.Y. Jan. 18, 2022) (finding that the Commission had plausibly alleged that the defendants were dealers “for the



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simple fact that” their trading, “in fact, involved buying and selling securities”); *SEC v. Almagarby*, 479 F. Supp. 3d 1266, 1272 (S.D. Fla. 2020) (“[T]he centerpiece to the definition of dealer is the word ‘business,’ and . . . where a company’s business model is based entirely on the purchase and sale of securities, that fact constitutes conclusive proof that the company is a dealer.”).

This enforcement activity threatens to throw the broader market into disarray. The Staff’s enforcement theory calls into question the legality of most of modern American finance, as a large proportion of firms that trade securities—including as their *sole* business activity, such as hedge funds—are not, and have never been, registered as “dealers.”

Already, the Staff’s enforcement activity has caused enormous hardship for the SPCC’s members. The SPCC is the voice of small public companies—firms that employ thousands of Americans developing new and innovative products and services. The Coalition’s mission is to protect this industry, and the financial professionals who serve it, from harmful government interference that suppresses growth, hinders capital formation, and eliminates jobs.¹ Unfortunately, the Commission’s enforcement Staff has wielded its expansive conception of “dealing” in an attempt to eliminate a vital source of financing for small public companies: market-adjustable convertible securities. As the SPCC has explained in detail elsewhere (and incorporates by reference here), market-adjustable convertible securities offer small public companies a quick, affordable way to finance their nascent operations—to pay their employees and vendors, and to set themselves up for future success. *See* Comments of the Small Public Company Coalition on the Proposed Amendment to Rule 144, File No. S7-24-20 (Mar. 22, 2021).² The enforcement Staff has tried to all but eliminate this critical source of capital by claiming that market-adjustable convertible investors are actually unregistered securities “dealers”—all because they acquire convertible securities and (months later) sometimes sell shares. *See, e.g., Carebourn Cap.*, 2022 WL 1639515; *SEC v. Keener*, 2022 WL 196283 (S.D. Fla. Jan. 21, 2022); *SEC v. Fife*, 2021 WL 5998525 (N.D. Ill. Dec. 20, 2021).

The enforcement actions against the convertible lending industry—premised on the Staff’s expansive conception of dealing—have dried up what the Commission itself admits is a critical form of financing for small public companies, raising firms’ cost of capital and driving many into bankruptcy. *See, e.g., Rule 144 Holding Period*, 86 Fed. Reg. 5063, 5073 (Jan.

¹ An important function of the SPCC, therefore, is to represent the interests of its members in matters before Congress, the courts, and the Executive Branch. To that end, the SPCC comments on—and if necessary, challenges—rulemakings, such as the present one, that threaten the ability of small public companies to obtain the investment capital they need to establish themselves, grow, and ultimately thrive.

² Available at <https://www.sec.gov/comments/s7-24-20/s72420-8530449-230302.pdf>.



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19, 2021) (acknowledging that limiting the availability of market-adjustable convertible notes will “prevent some unlisted issuers from obtaining financing or increasing the costs of doing so”); *see also* Letter from H. Walker, Gibson, Dunn & Crutcher LLP 2-4, File No. S7-24-20 (Oct. 4, 2021)³ (documenting more than \$4 billion in current market capitalization that would likely not exist today had an earlier Commission eliminated market-adjustable convertible financing).

It does not need to be this way. Instead of proposing a “further defin[ition]” of the term “dealer” to sweep in firms that “perform functions *similar* to registered dealers,” 87 Fed. Reg. at 23,056, or finding dealer status on a purely quantitative basis, *see id.* at 23,071, the Commission should instead strive to identify the “standards of activity” that indicate what dealers actually *are*, *id.* at 23,077. To do so, the Commission should—in fact, must—look to the definition of “dealer” Congress has already provided. *See Chevron USA Inc. v. Nat. Res. Def. Council*, 467 U.S. 837, 842-43 (1984) (“If the intent of Congress is clear, that is the end of the matter, for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress.”).

Congress’s definition of “dealer” was not “drawn broadly.” 87 Fed. Reg. at 23,057. Quite the opposite. When Congress enacted the Exchange Act in 1934, it defined “broker” and “dealer” in parallel terms, in back-to-back sentences:

(4) The term “broker” means any person engaged in the business of effecting transactions in securities for the account of others

(5) The term “dealer” means any person engaged in the business of buying and selling securities for his own account

Securities Exchange Act of 1934, ch. 404, § 3, 48 Stat. 881, 883. These definitions have remained materially unchanged for nearly ninety years. *See* 15 U.S.C. § 78c(a)(4)(A), (5)(A)-(B). Supreme Court precedent requires that these words be given their plain, original meaning “at the time of the Act’s adoption,” *New Prime Inc. v. Oliveira*, 139 S. Ct. 532, 539 (2019), and “be read in their context and with a view to their place in the overall statutory scheme,” *Util. Air Regulatory Grp. v. EPA*, 573 U.S. 302, 320 (2014).

Interpreted in that light, the congressional definition of “dealer” is clear: it refers to a public securities business that serves investors by effectuating customer orders. *See XY Planning Network v. SEC*, 963 F.3d 244, 248 (2d Cir. 2020) (“Broker-dealers effect securities transactions for customers”). By the time Congress enacted the Exchange Act, the concept of

³ Available at <https://www.sec.gov/comments/s7-24-20/s72420-9323318-260148.pdf>.



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brokers and dealers had a “long [and] continued executive construction,” *Oil Shares, Inc. v. Comm’r*, 29 B.T.A. 664, 669 (1934), and had “been before the courts for adjudication repeatedly,” *Johnson v. Winslow*, 279 N.Y.S. 147, 156 (Sup. Ct. 1935), *aff’d*, 246 A.D. 800 (N.Y. 1936). Then, as now, everyone understood that a broker would buy and sell securities “for” his customer, as the customer’s agent, whereas a dealer would buy and sell securities “from” and “to” his customer, as a principal. C.H. Meyer, *Law of Stock Brokers and Stock Exchanges* § 43-a, at 32–34 (1933) (“Law of Stock Brokers 1933”).

In ordinary parlance, this distinction between brokers and dealers was expressed in terms of whose “account” facilitated the customer’s trade. A broker, acting as the customer’s agent, would be said to trade “for the account of the customer.” SEC, *Report on the Feasibility and Advisability of the Complete Segregation of the Functions of Dealer and Broker*, at XIV (1936) (“SEC Report 1936”). A dealer, in contrast, would be said to effectuate the customer’s trade by taking the opposite side in “his own account.” *Weisbrod v. Lowitz*, 282 Ill. App. 252, 255 (1935). In the 1930s, everyone, including the Commission itself, understood the “other’s account” versus “own account” language as distinguishing, in functional terms, how a broker or dealer effectuated its customers’ transactions. *See, e.g.*, SEC Report 1936, at XIV (“The characteristic activities of a dealer . . . [are that that he] sells securities to his customer . . . or buys securities from his customer In any such transaction *he acts for his own account* and not as an agent for the customer. . . . On the other hand, a broker employed to execute an order for the purchase or sale of securities is the agent of his customer. . . . The transaction is *solely for the account of the customer*” (emphases added)); *Law of Stock Brokers 1933*, at 32-34 (“[Th]e broker . . . acts as the customer’s representative in making a purchase from or a sale to a third party. However, there is nothing in the law which prevents a person from engaging in the business of buying and selling securities *for his own account* as principal. Such a person is a security dealer as distinguished from a broker. . . . He sells to his customers . . . securities which he has purchased *for his own account* elsewhere, or buys from his customers securities *for his own account* with a view of disposing of them elsewhere Stock brokers, on the other hand, usually couch their confirmations in language somewhat as follows: ‘We have this day bought *for your account* and risk,’ or ‘We have this day sold *for your account* and risk.’” (emphases altered)). When Congress used “own account” versus “other’s account” phrasing in the Exchange Act, it intended to, and did, retain the established meaning.

Other textual and contextual clues point in the same direction. As indicated above, the definitions of broker and dealer appear in the original act in back-to-back sentences, and both words are defined in generally similar terms and placed throughout the act as linguistic neighbors. *See, e.g.*, § 11(e), 48 Stat. at 892 (directing the Commission to study the feasibility of segregating “the functions of dealer and broker”). This is strong contextual evidence that “both terms refer to different forms of generally similar conduct,” *Bullock v. BankChampaign, N.A.*, 569 U.S. 267, 274 (2013)—different ways of effectuating a customer’s order.



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The common-law backdrop confirms this reading. “It is a well-established rule of construction that “[w]here Congress uses terms that have accumulated settled meaning under . . . the common law, a court must infer, unless the statute otherwise dictates, that Congress means to incorporate the established meaning of these terms.” *Neder v. United States*, 527 U.S. 1, 21 (1999). Even where a statute “abrogates the common law in certain respects,” courts must nevertheless “presume that Congress retained all other elements of [the common law] that are consistent with the statutory text.” *Universal Health Servs., Inc. v. United States*, 579 U.S. 176, 187 n.2 (2016); *see also, e.g., Neder*, 527 U.S. at 23-25. By the time Congress enacted the Exchange Act, the common law had developed well-established criteria for “distinguish[ing] the dealer from the [broker].” William O. Douglas & George E. Bates, *Stock “Brokers” as Agents and Dealers*, 43 Yale L.J. 46, 60 (1933). As then-Professor (and future Justice) Douglas explained in 1933, the entire common-law framework for identifying a dealer, relative to a broker, turned on evaluating the relationship between the putative dealer and its customer. *See id.* at 60-61 (looking to the “form of the confirmation . . . [as] evidence of a dealer-customer relationship,” the “fact that the customer is not charged any commission,” and transfers “to the customer”). Given this common-law backdrop, it is inconceivable that Congress, one year later, employed the terms “broker” and “dealer” with the intention to sweep in firms that did not work to effectuate customer orders.

What the Commission calls the “‘trader’ exception” confirms this understanding. 87 Fed. Reg. at 23,057. Section 3(a)(5)(B) of the Exchange Act excludes from the “dealer” definition any person that buys or sells securities “but not as a part of a regular business.” 15 U.S.C. § 78c(a)(5)(B). Congress did not invent that exclusionary phrase for the Exchange Act. Rather, Congress plucked the language from pre-existing Internal Revenue regulations, *see, e.g., Donander Co. v. Comm’r*, 29 B.T.A. 312, 313 (1933), and, in doing so, is “presume[d] to have “adopt[ed] the cluster of ideas” that were attached to the “body of learning from which [the phrase] was taken,” *Air Wisc. Airlines Corp. v. Hoeper*, 571 U.S. 237, 248 (2014). That body of learning unquestionably excluded from dealer status any firm that did not buy and sell securities in order to facilitate customer orders. *Compare, e.g., Harriman Nat’l Bank v. Comm’r*, 43 F.2d 950, 952 (2d Cir. 1930) (a dealer “purchased securities to fill specific orders” and “h[eld] them for customers”), *with Oil Shares*, 29 B.T.A. at 668 (an “investment business,” which “buys and sells shares of stock” for “its own profit,” “is not a dealer in securities”). This understanding has been understood for decades, with every private investment fund, venture capital fund, hedge fund, and private equity fund relying on this understanding to correctly conclude that it is not required to register as a “dealer.”

The broader statutory structure further undercuts any notion that a dealer includes all businesses that buy and sell securities, regardless of whether they do so to facilitate customer orders. The entire regulatory regime is premised on the existence of customers. A dealer must, among other things, provide “notice[s] to its customers,” 15 U.S.C. § 78o(e), meet “financial



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responsibility” standards for the “custody and use of customers’ securities,” *id.* § 78o(c)(3)(A), and join a fund to insure the “dealer’s obligation’s . . . to each of its customers,” *id.* § 78fff-4(c). This makes perfect sense for firms that furnish the services usually provided by dealers, such as “solicit[ing] investors and handl[ing] their money and securities,” *In re Sodorff*, 1992 WL 224082, at *5 (Sept. 2, 1992), but is entirely nonsensical for firms—like convertible lenders—that do not.

The Commission’s inability to articulate a coherent and comprehensive definition of a dealer is yet another strike against the Commission’s interpretation. The Commission admits that without various regulatory exemptions, the proposed definition would sweep far too broadly, covering, for example, registered investment companies. *See, e.g.*, 87 Fed. Reg. at 23,094. That this exemptive “cure was needed” at all ““should have alerted [the Commission] that it had taken a wrong interpretive turn.”” *Chamber of Commerce v. Dep’t of Labor*, 885 F.3d 360, 383 (5th Cir. 2018) (quoting *Util. Air Regulatory Grp.*, 573 U.S. at 328). Other warning signs abound. The Commission is interpreting a *criminal* statute. *See* 15 U.S.C. § 78ff(a); *see Leocal v. Ashcroft*, 543 U.S. 1, 11-12 n.8 (2004) (explaining that if a statute has criminal applications, the “rule of lenity applies” to the Court’s interpretation even in a civil case, “because we must interpret the statute consistently, whether we encounter its application in a criminal or noncriminal context”). Yet, after 53 pages in the *Federal Register*, the Commission is *still* unable to definitively say what a dealer is. “[E]ven if [a firm] do[es] not” do any of the activities listed in the proposed rule, the Commission asserts that the firm “may *still* be acting as a dealer.” 87 Fed. Reg. at 23,062 n.87 (emphasis added); *compare, e.g., id.* at 23,105 (defining a dealer as a firm that earns “revenue primarily from capturing bid-ask spreads”), *with id.* at 23,069 n.159 (claiming that a firm “may be acting as a dealer by profiting from a spread even if they are not profiting from ‘bid-ask spreads’”). That is absurd. It does not take 53 pages to define a term that has criminal application—and even then, only to do so in a completely open-ended way.

In short, the Commission should abandon its flawed conception of what a dealer is (or what functions might be “similar” to that of a dealer) and instead adopt a regulatory definition that gives effect to the plain, original meaning of Congress’s definition: a public securities business that serves investors by effectuating customer orders.⁴

⁴ In accordance with the statutory text, the Commission should further limit the proposed definition to firms that buy and sell the *same* type of security, in the *same* form, at around the *same* time—which convertible note lenders do not do. The Exchange Act employs the conjunctive—“buying *and* selling.” 15 U.S.C. § 78c(a)(5)(A) (emphasis added). At the time the Exchange Act was enacted, that conjunctive phrase, when used in the context of state laws regulating dealers, was widely understood, “by coupling the two acts of buying and selling” together, to “render the law more explicit,” such that a dealer would include those entities that “buy and sell the same article in the same condition.” *State v. Yearby*, 82 N.C. 561, 562 (1880). That reading is consistent with the



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Respectfully submitted,

/s/ Marc A. Indeglia

Marc A. Indeglia
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common-law backdrop, and is presumed to reflect the meaning Congress intended. *See, e.g., Pub. Printing*, 1903 WL 3830, at *1 (Pa. Att’y Gen. 1903) (“In law, a dealer is one who buys and sells the same articles in the same condition.”).

The conjunctive “buying and selling” also conveys a temporal element. The buy and sell must have a “certain temporal proximity.” *Lake Building Prods., Inc. v. Sec’y of Labor*, 958 F.3d 501, 505 (6th Cir. 2020). As the Commission itself has recognized, the “conjunctive ‘buying and selling’” suggests that “concepts of two-sided markets” are relevant to the Exchange Act’s dealer definition. *Further Definition of “Swap Dealer,”* 77 Fed. Reg. 30,596, 30,607 (May 23, 2012). Concepts of two-sided markets connote a degree of “offsetting,” which necessarily entails a rough temporal proximity between the buys and sells. *Id.* at 30,607 n.174.